UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK
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COMMODITY FUTURES TRADING COMMISSION,

Plaintiff,

v. 22 CV 3401 (JPO)

ARCHEGOS CAPITAL MANAGEMENT LP, et al.,

Oral Argument

Defendants.

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SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v. 22 CV 3402 (JPO)

SUNG KOOK HWANG, et al.,

Defendants.

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New York, N.Y.
May 4, 2023
11:00 a.m.

Before:

HON. J. PAUL OETKEN,

District Judge

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(Case called)

MR. MURPHY: Good afternoon, your Honor. John Murphy, on behalf of the Commodity Futures Trading Commission.

THE COURT: Good morning.

MR. MURPHY: I'm joined by Alejandra de Urioste, Benjamin Rankin, and Jacob Mermelstein. I also would like to note that our general counsel, Robert Schwartz, is in attendance as well. He is not admitted in the S.D.N.Y., but is available to answer questions if the Court desires.

THE COURT: Good morning.

COUNSEL: Good morning.

THE DEPUTY CLERK: For Defendant Archegos Capital Management LP.

MS. LAWRENCE: Good morning, your Honor. Carmen Lawrence, King & Spalding, on behalf of Archegos. And with me today is William Johnson, also of King & Spalding.

MR. JOHNSON: Good morning, your Honor.

THE COURT: Good morning.

THE DEPUTY CLERK: And for Defendant Patrick Halligan?

MR. HAGGERTY: Good morning, your Honor. Tim Haggerty, from Friedman Kaplan Seiler Adelman & Robbins, for Mr. Halligan. I'm here with my partner, Mary Mulligan.

THE COURT: Good morning.

MR. HAGGERTY: I also wanted to let the Court know that our colleagues, Bonnie Baker and Anil Vassanji and Rupita

Chakraborty, are in the courtroom today, as is Mr. Halligan.

THE COURT: Good morning.

THE DEPUTY CLERK: For the SEC?

MR. ZETLIN-JONES: Good morning, your Honor. David Zetlin-Jones, from the Division of Enforcement. With me is Jack Kaufman, and also with me is David Lisitza, from our general counsel's office, who is available to answer any questions on the amicus brief filed in the CFTC matter.

THE COURT: Good morning.

THE DEPUTY CLERK: For Defendant Sung Hwang?

MR. LUSTBERG: Good morning, your Honor. Lawrence S. Lustberg, from Gibbons PC, on behalf of Mr. Hwang. With me is my partner, Thomas R. Valen, and many others who are seated in the audience and need not be introduced at this point.

THE COURT: Good morning.

I think that's it. Is there anyone else who wants to be identified?

All right. Good morning, everyone. I'm Judge Oetken, and there was a request for oral argument on the motions in this case. I know there was a request for guidance as to how to structure this. Unfortunately, I didn't really get into the briefing until the last few days because I was on trial, and I wasn't in a position earlier than the last couple of days to give guidance on that.

What I think would be most helpful for me is to break

it down into, I think, three issues, and then hear from whoever wants to speak about those three issues: First, the market manipulation claims; second, misrepresentations to counterparties; and then, third, issues relating to the CFTC complaint and specific issues relating to CFTC jurisdiction versus SEC jurisdiction, and how that impacts the motion to dismiss the CFTC's complaint.

I think we have about an hour, so I'd like to -- I don't want you to go on and on. And I will say that I did read the transcript of the oral argument before Judge Hellerstein in the criminal case and, obviously, saw his order denying the motion to dismiss the indictment in that case.

But let's start with the issue of market manipulation. I don't know who wants to start, either Mr. Lustberg or Ms. Lawrence.

MR. LUSTBERG: I think I'll start, if it's okay, your Honor.

THE COURT: Sure.

MR. LUSTBERG: Your clerk kindly told us we can be seated, but I'm old-fashioned, so I like to stand, if that's okay.

THE COURT: That's okay as long as we can hear you. These mics are actually made for sitting, but that's fine, as long as we can hear you.

MR. LUSTBERG: Thank you.

Your Honor, I will assume, as I speak today, that you have read everything, and I'm certainly not going to reiterate it, but there are just a few points I'd like to make.

Let me start by saying that you noted that you had read the transcript of the proceedings before Judge Hellerstein, as well as his decision. Obviously, we'll talk about this a little more, I think, as the day goes along — and we've written to the Court — but we don't believe that that binds the Court, it's a very different standard, and if you read the transcript, you know that Judge Hellerstein treated it as a very different standard than the one that's before your Honor on this motion to dismiss the civil case.

THE COURT: On that topic, let me just ask you at a high-level. It's obviously common, when there are parallel criminal cases and SEC or CFTC cases, to stay the latter because it's a different ultimate proof standard, even though the motion to dismiss standard may be different and criminal cases don't have *Twombly* and *Iqbal*, they don't have Rule 9, et cetera, but if there's a conviction, wouldn't that have preclusive effect? Because, for example, if the jury found beyond a reasonable doubt that there was market manipulation on the part of your client, wouldn't that be preclusive in a case where the standard is preponderance?

MR. LUSTBERG: Right. Well, there's no question that criminal convictions have collateral estoppel type effects

under certain circumstances assuming that all of the same issues were presented, all the same elements were met, and so forth, which appears to be the case here.

That is one reason why cases are stayed. As I note, your Honor is aware, the other reason cases are stayed have to do with Fifth Amendment rights, and, of course, our position is that those are not yet implicated; that is, we're at the point of arguing legal questions, at the point at which either we would be seeking to potentially depose government witnesses, presumably, and I don't think they have moved to stay, and they would have an argument. To the extent that they were seeking facts from us, we would have Fifth Amendment concerns, and we might have an application for a stay. But for purposes of this motion practice, for sure, there are inefficiencies in kind of doing it twice. But because there is this other enforcement proceeding out there, because it's the kind of thing that we're all focused on, because the legal issues deserve the kind of airing that they can get under an *Iqbal* and *Twombly* standard, even if not under the more lenient standard of a motion to dismiss a criminal case, we think it's appropriate for your Honor to address them now.

THE COURT: Understood. I do think the U.S. Attorney's Office has moved to stay these cases --

MR. LUSTBERG: Yes.

THE COURT: -- at least with respect to discovery; is

that right?

MR. LUSTBERG: Yes.

And our position has been that motion for a stay is premature at this stage, that when we get to the point at which there will be discovery, at that point the Court should entertain that application. We'll set forth our position at that time. But right now, we're at a point where we're just looking at the legal sufficiency of the allegations.

THE COURT: Okay. Fair enough.

I didn't even give you a chance to start, really.

MR. LUSTBERG: I'm more than happy to have this made more of a conversation.

THE COURT: Right. So I want to direct you to the bigger questions I have.

On the market manipulation claims, I'm just going to give you my thoughts and let you respond, and my questions.

You cited some of the cases that talk about the principle that intent to create an artificial price, manipulate the market, is not enough, you need some additional deceptive conduct, et cetera, but when you look at the most recent Second Circuit cases, particularly *SET Capital* and *Vali Management*, as well as some of the district court cases like Judge Cote's decision — I think it was *Lek Securities* — they seem to say, at least in many circumstances, intent is enough, intent to manipulate the price, and we can argue about what that means,

but, basically, it means intent to manipulate the price where there's no economic reason to manipulate the price, but you're doing it for some other reason; it's not the supply and demand that the cases talk about.

If it's true that the most recent cases indicate that intent is enough, you basically have a set of circumstantial evidence, and a lot of the defendants briefing here is sort of questioning the basis for the inference that there's that intent.

So how do you respond to that set of issues?

MR. LUSTBERG: Let me unpack that into the two different questions that you asked.

The first has to do with the state of the law in the Second Circuit. Let me go right to precisely the cases that you mentioned.

So *SET Capital*, which the SEC -- and let me be clear for Mr. Hwang, we're only in the SEC case, not the CFTC case. So when I say the SEC, I'm not meaning to exclude my friends.

The SEC certainly quotes *SET Capital* for the proposition that open market transactions that are not inherently manipulative, they constitute manipulative activity when accompanied by manipulative intent, that is, intent alone is enough.

But, your Honor, we would urge you, as you read each of these cases, to think about at least three things, and I'm

going to go through them for each of these cases. The first is to look at the case as a whole; the second -- what I mean is what other things the Court says in those cases; the second is to look at the facts of those cases; and the third is to ask whether a definition of manipulative intent, which is what they say has to be shown, has been really provided so that it's a workable standard.

Let me take each of those with respect to just the cases you mentioned.

With regard to *SET Capital*, in addition to the quote that I just read you, *SET Capital* says this, and I quote: While a defendant may manipulate the market with open market transactions -- I should say that is something we do not dispute. And let me just parenthetically say, one of the things that the SEC points to throughout is an argument that a sort of strawman they try to set up and then knock down, which is somehow that we're arguing that open market transactions can never be the subject of manipulation. That is not our position, just to be clear. We're not saying that open market transactions can never be the subject of a manipulation claim. We're saying that there has to be the something more that your Honor referred to.

But anyway, back to the quote, it says, "While a defendant may manipulate the market through open market transactions, some misrepresentation or nondisclosure is

required." That's in *SET Capital*.

SET Capital also says, and I quote: "Deception is the gravamen of a claim for market manipulation."

The court in *SET Capital* does not actually define what the manipulative intent that would be alone enough to bring a claim would be, but it seems that what is meant is exactly what the court says, which is, an intention to deceive, an intention to send a false signal to the marketplace, and so forth.

I should also note that *SET Capital* itself was a case about deception. It was a case about deceptive offering documents. So you didn't really ever need to reach the question, and so it's dictum that matters as to whether or not manipulative intent was enough.

I know that the court said that, but the court said other things as well, and the problem that your Honor has, and the reason why your decision is such an important one, is with regard to each of these cases, you're going to have to reconcile the different things that the court said and then come up with a definition of manipulative intent. And our suggestion, respectfully, for what that definition is, or should be, is an intent to deceive by sending a false signal to the marketplace.

THE COURT: But why isn't that met by the circumstances where, as alleged, assuming the truth of the allegations in the complaint, there was an intent to deceive as

to the real market value of the securities by pumping them up artificially? Why isn't that enough, that level of generality?

MR. LUSTBERG: So there would have to be an intent to deceive and to send false signals to the marketplace, and what you're asking me now is whether the actions that are alleged in this complaint are enough. And you described them as pumping up the price of the security, but that's not actually, your Honor, what's alleged in this complaint. What's alleged in this complaint, and what makes this case so special, is that the various -- each of the various sets of facts upon which the SEC relies have to do with legal activity.

So, they say that you pumped up the stock by trading in swaps, and the market didn't know that you were in them because you don't have to disclose your identity in swaps. But that's completely lawful. The notion that swaps limit the visibility of market participants into the extent of Archegos' aggregate holdings, which is the precise allegation of the complaint, is one that, in essence, says, you know, the regulatory regime is wrong, swaps should be regulated in a way that they currently aren't. But, of course, that's not for this Court, and I should note — and we point out in our brief — that there is regulatory action now that would accomplish that, but it has not yet been finalized.

But, really, if you take the complaint as a whole and say this is all an effort to pump up stock, I get what you're

saying. But that's really not what it is. And what we say is that you have to break down each of the components of what's alleged.

So the first is the use of swaps, which do not require disclosure.

The second is that it was a highly concentrated portfolio. Again, nothing unlawful about that. It would be radical, indeed, and it is radical, their position, that somehow trading in large quantities in a highly concentrated portfolio is unlawful. It isn't.

They talk about time trades, premarket, you know, at the close of the trading day. Those things, as we've pointed out and we cited authority for your Honor, are also entirely lawful.

THE COURT: Right, but you go through all of the particulars of what they show was pumping up the stock, and say, that's not illegal, that's not illegal, that's not illegal, but the question is, under the circuit's law, whether there was this bad intent. When you put them all together, that's different than all those cases that say each one of those isn't enough.

MR. LUSTBERG: Respectfully, your Honor, what a dangerous way of looking at it. So you take legal act, upon legal act, upon legal act, and that somehow is rendered illegal based upon intent, which is undefined, it's manipulative

intent. So they would have to show -- and they claim they don't have to show this. That's the key to this complaint. Their argument is that if you show that Mr. Hwang's intent was simply to affect the price, one way or the other, then that would be sufficient. That is the part of their argument --

THE COURT: To artificially affect the price.

MR. LUSTBERG: Well, artificially means that there would have to be an artificial signal to the marketplace, and that's not alleged in this complaint. It's just not. Except to the extent that that artificiality is based upon lawful conduct.

So their argument is that there's artificiality because the market doesn't know that Mr. Hwang is trading in swaps, that he's behind the counterparties' transactions, and we can talk about whether that's a perfect one-to-one, but that may be more of a matter of fact. But the point I'm making is that the artificiality that they assign to the actions all is as a result of a hundred percent lawful activity.

I think your Honor is correct, and I think the SEC is correct — we are saying that each of the things that they allege is lawful. And their conclusion is when you take all those things together, which you have to do, and then layer in intent, which they don't define, and call it manipulative intent, but layer in an intent, which is to affect the price, that that's enough for a manipulation case, and, respectfully,

we think that's not what the cases say. We think it's not what *SET Capital* says. I'll address one other case that you mentioned, which is *Vali*, and in *Vali Capital*, again, they quote that same language that we talked about earlier, and they say that, in some cases, scienter is the only factor that distinguishes legitimate trading from improper manipulation. They do correctly quote the case for that. But what they don't quote is other aspects of the case, which is where the court upholds the jury verdict in that case because, "The charge clearly instructed that to find defendants liable for manipulative acts under the Exchange Act, the defendants must have engaged in an act that sends a false pricing signal to the market or creates a false impression of supply and demand," and defines scienter as the intent to deceive, manipulate, or defraud.

THE COURT: Well, that is exactly what the SEC alleged.

MR. LUSTBERG: No, it isn't, your Honor. No, it isn't. They claim that we do not have to show an intent to deceive, manipulate, or defraud. Their argument is that a mere intent to affect the price is enough to -- when you layer that on top of each of the otherwise lawful actions that Mr. Hwang engaged in. That is the essence of their argument.

There's the deception -- they may say that we think there's deception, but if you look at what the deception is,

the deception that they see is inherent in the acts that have been deemed to be lawful or unregulated. Again, I'll just go back to the swaps. The argument is that somehow Mr. Hwang created a misimpression in the marketplace that there were numerous participants when it was all just him. And that's the way he pumped up, to use your phrase, the stock. But that was lawful. If it was swaps, he didn't have to. And, by the way, the signal to the marketplace was the trading that was done by his counterparties, the banks.

And there's nothing inaccurate about that. The market didn't know that, and the market never knows when counterparties like that trade, what their intention is. Here, they say, well, they were just hedging on his trades, but who knows what their reasons were for any given trade. We don't know.

And that's in a way, your Honor, what this case is all about. What this case is all about is the idea that if the SEC is right, then any trade, that anybody ever does, could be deemed unlawful, even though each aspect of it is lawful, just because one's intent was somehow to do something other than whatever the regulators think it is.

Let me be really clear about that, because you said it well. The question in a way is whether there was -- the trades had an economic rationale. Well, as Judge Posner says in the case that you cited, the so --

THE COURT: The "so what" case.

MR. LUSTBERG: So what, yes.

THE COURT: Right, he says so what. But that's not the law in the Second Circuit. That might have been the law in the '90s, when Judge Posner was around. I think there's a "so what" answer here, which is in *SET Capital*, which is that perfectly lawful stuff can become unlawful based on intent alone. And it's intent to manipulate the price artificially. I agree that's a really hard question and might be a problematic precedent, and who knows what it means, but they did say it.

MR. LUSTBERG: And through deception and not -- through artificial price and deception. What *SET Capital* stands for, what *Vali* stands for, is there has to be a false pricing signal to the market, create a false impression of supply and demand, and the scienter is the intent to deceive, manipulate, or defraud. That's a high standard. And if the SEC wants to concede that that's the standard they have to meet, then we may be arguing past each other, but the way I read the SEC's papers, that is not their position.

THE COURT: Well, we have the SEC right here. Let's ask them.

MR. LUSTBERG: You'll get a chance to ask them.

THE COURT: I want you to wrap up because we don't have a ton of time. I want to give everyone a chance to speak.

But I get your argument, it's well made, it's certainly well made in your papers as well, as all the papers were.

Is there any final point or points you wanted to make?

MR. LUSTBERG: No, your Honor. If I may, can we have just a moment after they speak to talk about any point they might make?

THE COURT: Sure.

I'd like to give the SEC a chance to respond first on this market manipulation set of arguments.

MR. ZETLIN-JONES: Your Honor --

THE COURT: Mr. Zetlin-Jones, right?

MR. ZETLIN-JONES: David Zetlin-Jones, from the SEC.

-- I would just respond that I think your Honor framed up the issue well and framed the state of the law in the Second Circuit well; that is, open market trades that might be legitimate in other contexts can become actual manipulation when they are undertaken with manipulative intent.

THE COURT: Now, before I forget, I want to get your view on what Mr. Lustberg said, which is that the SEC's position is any intent to affect price is manipulation.

MR. ZETLIN-JONES: When transactions are undertaken for the purpose with the specific intent to move the price with price movement, price manipulation is the dominant purpose of the trade, yes, that constitutes illegal manipulation.

But one more point I want to emphasize, your Honor,

which is that this manipulative scheme had two essential and complementary components. One was the manipulative trading strategy — the high volume, timed buying, these total return swaps. But the other piece of it was the deception of Archegos' trading partners into selling the swaps that Archegos -- the volume of swaps that Archegos needed to achieve its manipulative effects, that is, to move the price.

THE COURT: So those are the two types of deception or manipulation?

MR. ZETLIN-JONES: To frame it up, I think the law is, under the circuit, under the cases you cited, intent alone can distinguish legitimate open market trade from illegal manipulation. There is no other act of deception needed. But even if there were, that deception is supplied by the succession of lies that Archegos, through Mr. Hwang and through Mr. Halligan, told to Archegos' counterparties to induce their trading in the securities.

In other words, your Honor, the market hedges that the counterparties made in the argument, that was not natural demand; that was artificial. It was a byproduct of the lies that Mr. Hwang and Mr. Halligan directed be told to the counterparties to induce their selling.

THE COURT: What's your response to Mr. Lustberg's argument that this just sweeps in so much kind of innocuous conduct, anytime the purpose of a trade is to affect the price

is perhaps broader than what we normally think of as market manipulation in the sense of kind of a noneconomic purpose?

MR. ZETLIN-JONES: I think the law of the circuit on this point is fairly clear. And while there could potentially, I could imagine, be some circumstances that create close calls, this just isn't one of them. We have a raft of circumstantial evidence proving up, shoring up, our allegations of manipulative intent, coupled with the admission of Archegos' head trader in the parallel criminal proceeding during its guilty plea where he acknowledged as much. And I think, in this case, the facts, as alleged, amply establish, for purposes of this motion, the intent that would be required.

THE COURT: Okay. Thank you.

MR. LUSTBERG: May I quickly?

THE COURT: Yes.

MR. LUSTBERG: Just three very quick points, and thank you.

THE COURT: Yes.

MR. LUSTBERG: First, I appreciate -- oh, were you not done?

MR. ZETLIN-JONES: No, no.

MR. LUSTBERG: Okay. I didn't mean to interrupt.

MR. ZETLIN-JONES: It's an awkward setup.

MR. LUSTBERG: Yes.

I think this has been a useful argument because what

you've heard the SEC say is that there doesn't have to be artificiality, that there doesn't have to be deception, all there has to be is an intent to move the price. And if intent to move the price is enough, then is it enough to have knowledge that the price will move? Because I can tell you, if I go to the corner store and buy a carton of milk, in some minuscule way, that's affecting the price of milk. Any trade affects price.

THE COURT: Right. But he said the dominant purpose has to be the moving of the price.

MR. LUSTBERG: Okay.

So even that, though, doesn't fold in any of the standards that -- I read to you from the same cases that they're citing that have to do with deception and artificiality, and I ask your Honor, as you review the allegations of the complaint, taking all of them as true, as you must, and leaving aside issues of plausibility, which my colleague will address, the question really becomes: Is any of the false signal -- is there a false signal, what's false about it, what false signal was sent to the market? And there's none that's specified. What deception was created? And I will come back to that really quickly in a second. But if the answer to those is embedded in lawful mechanisms, like swaps, like trades -- I mean, what they are saying is, yes, there has to be intent. But how you can tell that there's intent is the very

lawful conduct at issue.

So, just takes swaps. Yes, the market might be much more knowledgeable if the market participants understood who was investing in swaps — that's true — but it's not required. And if that's the basis for the argument that there's deception or a false signal being sent, then that can't be a complaint that can stand, and we've cited cases that say that, so I'll stop.

One last point: The deception that the SEC talks about, and the only deception that they've mentioned today, is false statements that are alleged to have been made with two counterparties. Those allegations, too, must be taken as true. There's jurisdictional arguments that have been raised about whether they're in connection with securities, but leave that aside for the moment.

Those statements to counterparties are not false signals to the market. If true, they're false statements to counterparties. And that's really the essence of our argument. I'm not sure we made it as crisply as we should have, so I want to be clear now. Our argument is, with regard to those, those have nothing to do with deception of the marketplace, with natural forces of supply and demand. Those have to do with false statements to counterparties. We can fight about whether that's securities fraud, but the issue here is whether those are false statements to the marketplace, false signals. And,

respectfully, for the reasons we've set forth in the papers, we think --

THE COURT: Right. But on that point, just to push back a little bit, that seems a little cute or naive in the sense that, as alleged, assuming the truth of the allegations in the complaint, everyone knows that the counterparties are hedging -- are not hedging, but that they're purchasing the securities that are the swap reference, and, indeed, the purpose, as alleged, is to buy up these swaps that are long positions knowing that the counterparties will actually buy the stocks, thus pushing the price.

So it's not very attenuated to say that they're actually knowingly and intentionally affecting the buying of the security.

MR. LUSTBERG: Yes, this may tread a little on Ms. Lawrence's plausibility point, but, in essence, our argument is that nobody really knows why trades are made by the counterparties. In reality, counterparties hedge sometimes, they don't hedge other times, sometimes they hedge in part, and overall what they do — but now we're getting into factual stuff — overall what they do is they hedge their whole portfolio and not hedge trade by trade.

That allegation, I think, fails the plausibility test, but I'll let Ms. Lawrence get to that because that's what she wanted to address.

THE COURT: Okay.

MR. LUSTBERG: Really, the allegation that every single swap purchase is accompanied by a corresponding hedge is without basis.

THE COURT: Right, but I have to assume it's true.

MR. LUSTBERG: I understand. I understand the standard, but what *Iqbal* and *Twombly* say is you have to assess the plausibility of that.

THE COURT: Okay.

Ms. Lawrence.

MS. LAWRENCE: Thank you, your Honor. I will try not to cover the same material that Mr. Lustberg has covered for efficiency. But to start off, we do agree with Mr. Lustberg that the statute is a necessary element to establish a market manipulation claim.

But assuming for purposes of the argument that the SEC is correct in the law, and we believe that it is not, the SEC still must allege factual allegations that establish that there was artificial price or a false signal sent to the market. That is the definition of manipulation.

We believe that the SEC's factual allegations are still insufficient to state a market manipulation claim because they do not establish at all that there was artificial price or a false signal to the marketplace or that either of those was caused by Archegos.

I just want to start first with the point that the SEC, not all of its allegations are entitled to an assumption of truth. As the Court knows under *Twombly* and *Iqbal*, conclusory and labels and formulaic presentations of the elements of a cause of action dressed up as factual allegations don't warrant and don't deserve the assessment of truth at all.

And many of the SEC allegations are just that — they're labels and conclusions. And we cite to a number of examples in our complaint. I want to briefly highlight one today. If you focus on paragraphs 88 to 90 of the amended complaint, the SEC alleges that Archegos engaged in substantial trading during the end of the trading day, that is, marking the close, to push the prices of certain stocks upward. That is a conclusory statement, your Honor, and the two paragraphs that follow that simply summarize statistical analysis of the number of trading days over two stocks over a three-month period, and cite some summary statistics with respect to the equivalent number of shares.

That, by itself, does not establish marking the close. Marking the close is an improper trading device where a trader seeks to have an impact on the end-of-the-day closing price by getting as near to those last trades as possible. That is improper.

So, to allege simply during that large trading window of 30 minutes that Archegos engaged in trades, when that's a

time when liquidity is at its highest and many market participants are in the market at that time without anything more, does not establish marking the close. So that type of a conclusory allegation needs to be disregarded and not given the assumption of truth.

When you strip away those conclusory allegations, what are left are factual allegations that really do not establish market manipulation by Archegos.

Now, I just want to spend some time going through a few of these points.

First, at its very essence, the SEC alleges through allegations, as I said, that are conclusory or that are negative inferences upon inferences from the legitimate trading engaged in by Archegos or characterizing transactions as swaps, as if they were equity trades, but the essence of it is that Archegos manipulated the equity markets in Archegos' top ten holdings by entering into off-exchange total return swaps, and these are private contracts between Archegos and the counterparties that are off-exchange.

What that means is that by engaging in those swap contracts, there is no direct market impact. And as you noted, the SEC's allegations relate to the hedging by the counterparty, but as we have discussed in our briefs, it is uncertain whether the counterparties will, in fact, engage in hedging activity in response to those swap contracts. And we

cite to a number of examples that we believe the Court can take notice of because they are either integral to the complaint or matters of public notice or public filings and the like. And one is that in the CSX case, there was testimony by the head of the swaps desk that counterparties hedge against swap contracts in a number of ways and not always one to one, and not always at all, because they may engage in offsetting swap contracts.

You'll also have the Credit Suisse report that was done by Paul Weiss and is a matter of public record where --

THE COURT: But even that said, 85 percent of the time, they're engaged in offsetting hedges.

MS. LAWRENCE: That is true, your Honor. But, also, there was a study, a survey, by Pricewaterhouse — it was a while ago — that also talked about the number of times, I think 46 percent was a percentage, that showed up in that survey.

So the point is that there is not any kind of certainty around whether they hedge, how much they hedge, when they hedge, or how long they hold those hedges, your Honor.

And that flows into the other point — the SEC makes another conclusory allegation that Archegos obtained market domination. How, your Honor, does Archegos dominate the market in securities where it does not have ownership of more than 5 percent of that stock? These swap contracts, they don't bestow beneficial ownership of the stock.

THE COURT: But you can just play out a scenario where

they only have 5 percent actual equity, but they engage in swap contracts in Viacom that, if you add on what they economically get from the swap contracts, they get 60 percent, and let's say even 85 percent of the hedging is going on by the counterparties, that gets to market control, pretty much.

MS. LAWRENCE: But, your Honor, it isn't market control because that's economic benefit or risk. Market control is about stock ownership and being able to have control over those securities.

You don't know day one if they hedge. Next day, they could have sold those securities and entered into offsetting swap. And proof in the pudding, your Honor, is that week of March 23rd, Archegos collapsed because it had no control of those securities and those owner market forces at work, and the price declined. If Archegos had control of those securities — 70, 80 percent — that would not have happened.

THE COURT: But that also cuts the other way, I think, because the fact that it collapsed shows how much they were dependent on these particular top ten securities.

In any event --

MS. LAWRENCE: But there are many funds that concentrate in a small number of securities, and it is true that had they not concentrated as much, then, obviously, those price declines, which were the result of external forces having nothing to do with Archegos, wouldn't have impacted.

THE COURT: At the end of the day, it's true that these allegations have to be plausible under *Twombly* and *Iqbal*, and they can't be conclusory, but when you add them all together, I do think they're more than any particular one in terms of getting to the intent that is required under the case law.

I want to give them a chance to respond, but finish your point.

MS. LAWRENCE: I just want to get to the intent, because I think the difficulties with the SEC's argument that if you take this legitimate trading activity, whether individually or collectively, it rises to a strong inference of scienter, that is not plausible, your Honor. It's not plausible because nothing in the legitimate trading activity is inherently deceptive.

So what the SEC is saying is, the reason there's manipulation here is because of all of this legitimate trading activity and with manipulative intent, and the way we prove our manipulative intent is with all of these legitimate trading activities. That is circular, and it's an argument that lacks substance, your Honor. It just makes no sense.

The other thing is that the SEC points to the allocutions of former employees of Archegos and Will Tomita, the former trader, as the only one that's relevant here. We think that for the same reasons that some of the SEC's

conclusionary allegations shouldn't be afforded the assumption of truth, the same with respect to Mr. Tomita's allocution. It is surprising in its lack of factual matter. All it does is recite elements of a manipulative claim and, therefore, does not constitute factual matter that should be afforded the assumption of truth.

And moreover, the SEC has pled that it's Mr. Hwang that had the decision-making control over the trading decisions of Archegos, and that Mr. Tomita was just following instructions and did what he was told, and given that and Mr. Tomita's insignificant role in the legitimate trading at Archegos, it should be afforded minimal weight.

THE COURT: Thank you.

Do you want respond to those, Mr. Zetlin-Jones?

MR. ZETLIN-JONES: Sure.

Just very briefly on the issue of hedges, I think paragraphs 37 to 39 of the complaint allege plainly and clearly that counterparties, as a matter of common practice, would hedge their total return swap exposures by buying the equity shares in the market.

And Ms. Lawrence referenced the testimony provided in the CSX case. I would urge your Honor to look at what the CSX court found, which found that, as a practical matter, it is inevitable that counterparties will hedge their total return swap exposures by buying underlying shares in the market.

And Judge Winter, in his concurrence, on appeal of that matter, said, although shorting -- the other hedging methods for short parties exist, they are exceptional, and he noted, a short party's purchasing of shares is the most practical and common method of hedging, and long parties expect that it will be used.

I guess the only other point I would address, your Honor, is this notion that Mr. Tomita's allocution as Archegos' head trader --

THE COURT: Could you come a little closer to the mic?

MR. ZETLIN-JONES: Yes.

-- that Mr. Tomita was Archegos' head trader, not a junior employee, that his allocution should be given little weight, that is an argument that goes, on its face, to the weight of the witness credibility and isn't appropriate for consideration on a motion --

THE COURT: They argue it's just conclusory, that it just says the elements of the --

MR. ZETLIN-JONES: He's a percipient witness to the scheme, he was a critical participant in it, and he affirms the intent with which these trades were undertaken, and his account is borne out by the trading patterns that the complaint proceeds to allege.

THE COURT: Would you respond briefly to the argument that Ms. Lawrence and defendants have made about the

plausibility of the timing, that it's just looking at the last 30 minutes isn't really meaningful to close out the day as opposed to sort of the very end of the day, and then sort of looking at several months, there was X amount of trading on X days as opposed to a more robust analysis of the entire period, that that isn't enough to get plausibility?

MR. ZETLIN-JONES: So, as we allege, the entire course of conduct was designed to prop up these prices; that is, the massive buying, the accumulation of 50, 60, 70 percent of freely tradeable outstanding shares of this company, was all of a piece. And the examples that we highlight — of late trading, of setting the tone, of latter trade, trading in response to negative news to counteract selling pressure — those are all the features of the transactions and examples we give to support, strengthen, the inference that this trading was being undertaken with the intent to acquire.

THE COURT: You probably weren't there for the Judge Hellerstein argument in the criminal case, but he asked something that I was also curious about, which was kind of, what's the theory of the end game here? This isn't like Credit Suisse or something where there was kind of an immediate benefit to Archegos or Mr. Hwang from driving up the price, as alleged. As he said, at some point, the bubble bursts, so what exactly is the motivation, the self-interested motivation, that would be behind a theory that this kind of manipulation is

going on?

MR. ZETLIN-JONES: Yes, your Honor.

THE COURT: Was it kind of a mania that didn't really have much rational thinking behind the end game? Was it kind of desperation? What was the thinking?

MR. ZETLIN-JONES: I think it was a combination of those, your Honor. We allege — and I don't have the paragraph offhand — we allege that his portfolio took a big hit at the start of the pandemic. It was way out. As referenced at the argument before Judge Hellerstein, I think there was a drive, an ego, a desire, to be among the most wealthy people in the world, and, as we allege in our complaint, he did, in fact, explore and look for off ramps, a way to lock in the profits achieved through manipulation, but was just unsuccessful in doing so.

And toward that end, a lot of the manipulative trades that were going on were just buying time, keeping the music going for as long as he could, which, your Honor, is not unusual in manipulative schemes. Oftentimes, people will undertake manipulative schemes that seem, from the start, to be doing that.

THE COURT: Thank you.

I want to turn to the set of issues involving misrepresentations made to counterparties, which I think is the other big theory, and this one implicates the claims involving

Mr. Halligan.

Do you want to take that on, Mr. Haggerty?

MR. HAGGERTY: Thank you, your Honor.

I'll address the Court from the podium, if that's acceptable.

THE COURT: Sure.

MR. HAGGERTY: Your Honor, Tim Haggerty, for Patrick Halligan.

I'll address three issues principally with respect to the misrepresentation allegations, and these are well briefed, so I'll try to be efficient.

First, I'll address why the regulators haven't sufficiently alleged --

THE COURT: You're complimenting your own briefing?

I agree, it was well briefed.

MR. HAGGERTY: So stipulated, your Honor.

So, the first issue is whether the regulators have sufficiently alleged that misrepresentations were made in connection with either SEC-regulated securities, purchases, or sales, or CFTC-regulated swap transactions.

The second issue is whether the regulators have sufficiently alleged that Mr. Halligan made misrepresentations, as would be required for a maker liability claim under 10b-5(b) or the parallel provision of the Commodity Exchange Act and its regulations.

The third issue is whether the regulators have sufficiently alleged a scheme liability claim against Mr. Halligan, and, in particular, the application of the Second Circuit's recent decision in *SEC v. Rio Tinto plc*, which holds — and we think it's dispositive of this case — that a plaintiff can't simply repackage misrepresentation claims and call it a scheme.

So, those are the three issues, but I did want to briefly note that I was surprised to hear Mr. Zetlin-Jones refer to Mr. Halligan during the discussion of the market manipulation allegations, because, as we read the SEC's complaint, there's certainly no well-pled allegation that Mr. Halligan engaged in any deceptive conduct with respect to the alleged market manipulation.

And Mr. Halligan is described as — this is paragraph 25 of the complaint — as a back-office professional, and he's not described to have had any role in trading, his name isn't mentioned in the pages or paragraphs describing the market manipulation allegations. So we do respectfully submit that the market manipulation allegations should be given absolutely no consideration with respect to the sufficiency of the regulators' claims against Mr. Halligan, whether that's under a maker liability theory, a scheme liability theory, or it's with respect to the assessment of his scienter.

I'll turn now to the in connection with issues, and

they arise in both cases.

What I would highlight is that there's a real difference between the positions advanced by the defendants and the positions advanced by the regulators. As I see the difference, it's that the defendants have offered the Court a standard to apply the in-connection with requirement that's consistent with the most recent decisions of the United States Supreme Court — that's *Chadbourne & Parke v. Troice* — and as well as the most recent decision of the Second Circuit interpreting the in-connection with language of the Exchange Act. That's *Charles Schwab v. Bank of America*.

What the rule is — and it's a workable standard — is that a misrepresentation is actionable and in connection with the securities purchase or sale if the misrepresentation concerns the value of a security being traded or the consideration received in exchange for the security.

I'll read what the Second Circuit wrote in *Charles Schwab* because it's really quite explicit. "A claim fails where the plaintiff does not allege that a plaintiff misled him concerning the value of the securities he sold or the consideration you received in return."

The SEC and the CFTC cite a number of cases that contain sound bites, which we respectfully submit are taken out of context, that might describe individual characteristics of those particular cases, but don't constitute a workable

standard. And, in fact, the cases that the SEC and the CFTC rely upon are entirely consistent with the standard that the Second Circuit described in *Charles Schwab*. For example, both of the regulators rely extensively on the case, the Supreme Court's 2002 decision in *SEC v. Zandford*. And *in Zandford*, the issue was whether the facts were their broker made unauthorized transactions, unauthorized sales, in a customer's securities trading account and then misappropriated the proceeds. It's really nothing like this case. It's not even an affirmative misrepresentation case in the way that this case has been alleged.

But, in any event, the deception in *Zandford*, these unauthorized trades in the customer's discretionary securities account, did, in fact, coincide with the securities transactions — they, in effect, were the securities transactions — but it also fundamentally related to the consideration that the customer received for those transactions because the deception deprived the customer of the consideration. It's entirely consistent with the rule that we've advanced.

THE COURT: Why couldn't it be the theory that alleged misrepresentations regarding makeup of portfolio, other characteristics of the portfolio that Archegos had, were crucial, and I guess but for those misrepresentations, the swap would have been uninteresting, unpalatable, to the

counterparty, and, in that sense, it affects the value of the swap?

MR. HAGGERTY: Well, at least a few responses to that, your Honor.

The first is -- and your Honor used the phrase "but for." And that is a rationale that's entirely foreclosed, we believe, by the Second Circuit's decision in *Chemical Bank*, *Chemical Bank v. Arthur Andersen*, where the Second Circuit expressly held that but-for causation, that is, but for the alleged misrepresentation, a securities transaction wouldn't have occurred, that that's not a sufficient way for a plaintiff to satisfy the in-connection with requirement.

Additionally, the alleged misrepresentations regarding characteristics of the portfolio, at most, relate to the assessment of counterparty risk, not a characteristic of the value of the securities, not a characteristic of the consideration received for the securities, and they were made — and this is as alleged in the complaint — the alleged misrepresentations were made during negotiations over capacity and margin — preludes to potential opportunities for future securities transactions.

THE COURT: What about the risk that I don't get the consideration? I'm the counterparty, these margin issues and the issues that misrepresentations involve make the likelihood I'll get the consideration, you know, higher than they would be

if I were told the truth. Isn't that relating to the consideration?

MR. HAGGERTY: Well, your Honor, I believe that argument runs directly into the Supreme Court's decision in *Chadbourne & Parke v. Troice*, where the misrepresentations related to the -- it was one of the Allen Stanford Ponzi Scheme cases, and there were misrepresentations made about the securities portfolio that was being held. And the argument that was made there was that the misrepresentations regarding the securities portfolio, which is like the allegations in this case, which are alleged to be about Archegos' securities portfolio, made doing business with the counterparty riskier. But that was held not to be sufficient in that case.

In other words, misrepresentations about counterparties' creditworthiness, which goes to general terms of the relationship -- which really relates to general terms of the relationship between the customer and the bank, isn't sufficient.

I also refer the Court, respectfully, to district court decisions, both affirmed by the Second Circuit, *Bissell* and *Levitin*, where alleged misrepresentations were made regarding what was described in those cases as terms of the relationship between the broker and the customer — in those cases, the misrepresentations related to interest that would be paid in connection with collateral deposited with short

securities transactions — held not to be sufficient.

Also, in response to the question that the Court just asked, there's also not an allegation in either of the complaints that Archegos made a misrepresentation about the risks of any future securities transaction, which is really different than what is alleged, which is misrepresentations -- alleged misrepresentations about the characteristics of the securities portfolio that Archegos presently held.

THE COURT: I think I understand the argument on in-connection with. Do you want to move to maker liability?

MR. HAGGERTY: Absolutely.

Your Honor, on maker liability, the Supreme Court's decision, United States Supreme Court's decision, in *Janus v. First Derivative Traders* holds that under 10b-5(b), the only person who may be primarily -- who can be held liable for a primary violation is the maker of the statement. So in --

THE COURT: This is the speech writer analogy?

MR. HAGGERTY: This is the speech writer. The court also uses the metaphor, it's less commonly discussed, but playwright, not the maker of a statement, that an actor delivers. And, as alleged here, the regulators fall short of the requirement of *Janus* because what they allege is it's really that someone else spoke the statements — that's principally Mr. Becker — made the statements to counterparties, but the regulators seek to hold Mr. Halligan responsible as the

maker for the statements that Mr. Becker actually delivered. But there's no well-pled allegation that Mr. Halligan had — and this is what *Janus* requires — ultimate control over either the content or the delivery of the statements that Mr. Becker made.

There is no authority cited for the proposition — and this is what we do submit the regulators are asking the Court to hold — that a supervisory relationship is sufficient to make a supervisor the maker of the statements that a subordinate delivers. That actually seems facially inconsistent with the facts of *Janus*, where the defendant was the advisor for a mutual fund, and the misrepresentations were made with respect to the mutual fund issued, but its advisor, the defendant, substantially participated in the preparation of and had substantial control over the fund.

THE COURT: Okay.

MR. HAGGERTY: If the Court has other questions on the maker liability issue -- your Honor, if I may, on maker liability, I should note that the CFTC appears to argue that *Janus* should not apply to the maker claim that has been asserted in that case. That argument fails for a host of reasons, the first of which, the Second Circuit has repeatedly applied *Janus* to claims brought by the SEC, enforcement actions brought by the SEC. There is no reason that the same result isn't appropriate with respect to claims brought by the CFTC. But, more fundamentally, in *Janus*, the question was what does

the work "make" mean, and the court defined the word make by looking at the dictionary and by looking at basic rules of grammar and syntax. And there is no reason — the CFTC offers none, they offer no case that says to the contrary — there's no reason that the word "make" shouldn't be given a common application when used in the context of the securities and commodities lawsuit.

THE COURT: Why don't you turn briefly to scheme liability.

MR. HAGGERTY: Sure, absolutely.

So, when the regulators filed their initial complaints in this action, it was unsettled in this circuit whether allegations relating to -- solely relating to the participation and the preparation of misrepresentations could sufficiently state a scheme liability claim. After the Second Circuit's decision in *SEC v. Rio Tinto* last July, it's clear that they can't. That's the explicit holding of that case. The Second Circuit's language is, "Allegations of misstatements and omissions alone are not sufficient to state a scheme liability claim." That was a direct rejection of the position that the SEC had advanced there. And we believe it is fatal to the claims, the scheme liability claims, that both regulators have asserted here because the claims, scheme liability claims, against Mr. Halligan are just a repackaging of the misrepresentation claims based on the allegation that he had

some role in participation in the preparation of those statements, whether it's by working with his colleagues or providing content, but those are all of the same things that *Rio Tinto* rejected as insufficient.

I point the Court to the recent -- there have been a number of decisions since *Rio Tinto*, including within the Southern District applying *Rio Tinto* to claims, and we referred to them in our brief — *In Re: Turquoise Hill* is one of them — and the statement there from Judge Liman is really clear: Where the only fraudulent conduct is the making of a false statement, the defendant is either liable as a maker or is not liable at all.

In this case, under the allegations as pled, Mr. Halligan is not liable as a maker under *Janus*, and he can't be liable under a scheme liability theory under *Rio Tinto*.

THE COURT: Okay. Thank you.

Anything else you want to add? I want to give them a chance to respond.

MR. HAGGERTY: No, your Honor, although I would ask for, if it's acceptable to the Court, the opportunity to respond.

THE COURT: All right. Great.

MR. HAGGERTY: Thank you.

THE COURT: Who wants to go first, Mr. Murphy or the SEC?

MR. MURPHY: Your Honor, I'm happy to go first.

THE COURT: Okay. You're welcome to.

Mr. Murphy, right?

MR. MURPHY: Yes, Mr. Murphy.

Your Honor, I intend to speak on the in-connection with element, and my colleague, Mr. Rankin, will speak on issues relating to maker and scheme liability.

THE COURT: All right.

MR. MURPHY: One thing I want to start with --

THE COURT: Could you pull the mic just a little closer?

MR. MURPHY: Yes, your Honor.

THE COURT: Thanks.

MR. MURPHY: One point I'd like to start with is the point that swaps are very different from your standard securities transaction. Unlike a share of stock, swaps are bilateral contracts that extend over a period of time — weeks or months or even years — and this has important implications for how to apply the relevant standards here for in-connection with. And due to these differences, among others, that the CFTC has stated that it will be guided by, but not controlled by, case law applying Rule 10b-5 in the Rule 180.1 context.

So, here, we've met both the standards under *Zandford* and *Chadbourne*. I want to start with *Zandford*, because we think that's the applicable standard here. The CFTC's

interpretive release under 180.1 specifically cites to *Zandford* as an applicable case, and defendants are trying to argue here that *Zandford* has been overruled or is somehow not good law, but that's just not the case. And, to the contrary, *Chadbourne* expressly left open the coincides standard, left that standard intact. The Second Circuit has cited the *Zandford* coincide standard as recently as 2021, and even after *Chadbourne* -- and even after *Chadbourne*, courts in this district routinely cite to the *Zandford* coincide standard.

THE COURT: That's sort of an odd standard — coincide with. That's like saying there's no connection, but they just happened at the same time. There's not much content to it.

MR. MURPHY: Your Honor, there is a bit more to it. In addition, the standard requires that the fraud and the swap or security are not independent events. And then in the Second Circuit's *Romano* case, it went into some more detail about how the coincide standard can be met.

So it can be met where a plaintiff's claims necessarily allege or necessarily involve, or rest on, a swap or a security, and it's met when the fraud induced a purchase or sale of the swap or security, and it's met where the misconduct and the swap are part of the same fraudulent scheme.

In terms of why we think *Zandford* is the more applicable standard here, particularly in the context of the Commodity Exchange Act, is that the CEA's antifraud provisions

are substantially broader than the SEC's. The terms value and consideration are most applicable to purchases and sales, which is all that is covered by Rule 10b-5, but Regulation 180.1 goes way beyond purchases and sales into territory where it doesn't really make sense to just talk about value or consideration.

So, for example, Rule 180.1 encompasses fraud in connection with solicitation, execution, pendency, termination, and all of the other payment and other obligations arising under a swap.

So if you focus just on value or consideration, as the defendants have argued, what you end up doing is cutting off a large portion of the conduct that Rule 180.1 was intended to prohibit.

Now, in terms of how we have met the *Zandford's* coincide standard, here, we're not alleging but-for causation; we're alleging inducement. Archegos' misrepresentations induced swap counterparties to enter into more broad-based securities index swaps. Whenever Archegos wanted to enter into long positions, it also needed to enter into the short CFTC swap positions.

So when Archegos made misrepresentations that induced additional long positions, those same misrepresentations induced additional short positions. We also allege the CFTC swaps here were an integral part of defendants' fraudulent scheme. That's because the counterparties used CFTC swaps as a

risk-reducing measure, and entering into these swaps was one of the many ways that defendants tried to falsely assure its counterparties that it was creditworthy.

Now, I want to turn to the *Chadbourne* standard, value in consideration standard, because we've met that as well. We are not alleging misrepresentations about the terms of a relationship. We are alleging misrepresentations about the value of these swaps. As I mentioned, a swap is an ongoing contractual relationship with ongoing payment obligations by the parties. So a misrepresentation about credit risk is a misrepresentation about the value of a swap.

I think your Honor made this point earlier — that the counterparties wouldn't have gotten the consideration that they expected here.

So, I also want to note that some of our allegations do relate directly to the attributes of the broad-based securities index. For example, we allege that Archegos' misrepresentations misrepresented the time that it would take to liquidate its entire portfolio, including the broad-based security index swaps.

And this case, your Honor, is a perfect example of how creditworthiness impacts the value of swaps as a result of Archegos' misrepresentations here, the swaps at issue, including the broad-based security index swaps were rendered essentially valueless.

I also want to briefly address the *Chadbourne* decision and the facts of that case. Defendants grossly misinterpret the holding of that case. This was a SLUSA case, and the outcome really hinges on the distinction between a covered security and an uncovered security under SLUSA. The defendants argue that this case stands for the proposition that misrepresentations about creditworthiness can never be in connection with a fraud. And that's simply incorrect as a matter of common sense and as a matter of law.

In fact, it was undisputed in that case that the representations about creditworthiness were in connection with securities. They just weren't in connection with covered securities. And that's the critical portion of that court's holding.

THE COURT: Thank you.

Do you want to turn to maker liability and scheme liability?

MR. RANKIN: Yes.

THE COURT: Mr. Rankin?

MR. RANKIN: Thank you, your Honor.

So I'll first address the issue of maker liability under *Janus*. I just want to highlight one point at the start, your Honor: We are not suggesting that Mr. Halligan is somehow liable solely because he's a supervisor of Mr. Becker. We're not alleging any kind of vicarious liability relationship.

What *Janus* tells us to look at is to look at the specific statement — who has control over that statement, who has ultimate authority over that statement, who controls whether to deliver it and how to communicate it?

In this case, your Honor, in our complaint, we've alleged at least four different statements that Mr. Halligan made through Mr. Becker. We also allege that Mr. Halligan made misstatements directly in these trade confirmations that he signed himself that falsely represented Archegos' beneficial holdings in various issuers.

With respect to the statements that Mr. Halligan made through Mr. Becker, I would point your Honor to paragraph 59, where Mr. Halligan told Mr. Becker to tell a specific swap counterparty, Swap Counterparty 3, that Archegos' largest position was 35 percent of its net asset value, which was false. Mr. Becker did so. Paragraph 63 and 64, where Mr. Halligan directed Mr. Becker to provide false liquidation statistics, including representing that Archegos could liquidate its entire portfolio, including the CFTC swaps, in 30 days to a specific swap counterparty, 4. That was false.

I would also point your Honor to paragraph 81, where Mr. Halligan proposed false talking points for Mr. Becker to use, then had a followup conversation where he specifically reviewed and approved those same talking points that Mr. Becker delivered to counterparties.

I don't see how you can show greater control over the specific message at issue than in those circumstances.

And, your Honor, we've also cited a number of cases in our brief in which one individual can make misstatements through another. *Lorenzo*, especially at the D.C. Circuit level, is a helpful example. The *Glickenhaus* case from the Seventh Circuit Court of Appeals is another. And there are others mentioned.

Unless your Honor has any questions over the *Janus* issues, I'll briefly touch on the scheme liability points.

THE COURT: Okay.

MR. RANKIN: So as counsel for Mr. Halligan has pointed out, under the *Rio Tinto* decision, there must be something beyond misstatements and omissions, but I just want to mention misstatements and omissions can still form part of a scheme. That decision doesn't say that misstatements and omissions cannot be part of a scheme. They can be part of a scheme. There just has to be something else, essentially.

And in the *SEC v. White & Case* and others, what we're looking for is some kind of deceptive actions that don't necessarily have to be illegal in and of themselves, but that contributed to a fraudulent scheme.

THE COURT: What is the "something more" here?

MR. RANKIN: The "something more" here as to Mr. Halligan -- first, I want to mention, again, Mr. Halligan

was the CFO at a small family Office, he was one of very few executives at this office, and he led or was one of the coarchitects of a scheme to systemically deceive swap counterparties as to Archegos' positions across various issuers. He did that in a number of ways, your Honor, as we alleged in the complaint. He concealed critical financial information in response to questions from counterparties. Concealment is a fact that comes up in a number of S.D.N.Y. cases as an example of deceptive conduct.

He also condoned the dissemination of false information by others, principally Mr. Becker, and he conspired with Mr. Becker and, at times, Mr. Tomita in undisclosed meetings and calls to further the scheme and avoid detection by counterparties. I point your Honor to paragraphs 63 and 64, which mention a call with Mr. Tomita and Mr. Becker; paragraph 76, where he essentially directed them to tell an inconsistent and misleading story to swap counterparties; paragraphs 59 and 67 and paragraph 81, where the three of them had a call to develop false information that Mr. Becker later provided to swap counterparties.

But I want to mention one more point, your Honor: An entirely separate basis for scheme liability is knowingly supervising an individual who is carrying out the fraudulent scheme. The facts of this case, as alleged in the complaint, certainly meet that standard. That's under the *SEC v. Collins*

& Aikman case.

Mr. Halligan knowingly supervised Mr. Becker in the carrying out of this fraudulent scheme. He ordered Mr. Becker to not disclose the true positions with counterparties, to conceal that information, he trained Mr. Becker to systemically lie about that information over years, and at various times, he made the comment, "if they only knew." And as we allege in our complaint, we think that that really shows it's a critical -- it's a critical admission of his culpable participation in the scheme — if swap counterparties knew the truth, they would have taken different countermeasures, but they didn't because they didn't have the full picture.

THE COURT: Thank you.

I want to give the SEC a chance to respond to Mr. Haggerty.

MR. ZETLIN-JONES: Sure. And I will try to keep this brief, your Honor, because Mr. Rankin has already touched on much of what I intended to.

On in-connection with, the only thing I would add in our matter is that the total return swaps that Archegos executed with its counterparties, those are securities — that's Section 281 of the Securities Act, Section 3810 of the Exchange Act — and there does not appear to be any dispute that those are secured.

THE COURT: The swaps themselves?

MR. ZETLIN-JONES: The swaps themselves are securities. So with that predicate, I think the in-connection with, the nexus between the misrepresentations and the securities transactions, it's pretty clear these lies induced counterparties to sell securities to Archegos. That's a straightforward, clear direct nexus as you can imagine.

We disagree that there is a subject matter limitation on the in-connection with standard. I think the *Charles Schwab* case, that they rely on this, was made in this particular context. That context was banks misrepresenting their borrowing costs to banks on the U.S. LIBOR panel, misrepresenting the borrowing costs to the British Bankers' Association, which had the impact of suppressing LIBOR. And there were two claims made by *Charles Schwab* there: One was that those misrepresentations affected or in-connection with their purchase or sale of floating rate instruments, that is, instruments that related to and reflected LIBOR, and the court in the Second Circuit affirmed that, yes, those misrepresentations are in connection with those instruments. Where *Charles Schwab* went too far was saying these misrepresentations, which had the effect of suppressing LIBOR, were also in connection with fixed-rate instruments that didn't reference or relate to LIBOR in any way, and it was only in that context that the court wrote a sentence that defendants have been relying on.

THE COURT: So, in general, you don't think that to be in-connection with, that it has to relate to the value of the securities or the consideration?

MR. ZETLIN-JONES: I think the standard is, as the Second Circuit articulated in *Romano*, it doesn't necessarily allege, necessarily involve, or rest on, your Honor, and I don't think there's a subject matter limitation. We cite a number of cases in our brief at page 56 and 57, where the misrepresentations did not relate to the value or the consideration, your Honor, but even if it did, for the reasons you have articulated in your colloquy with Mr. Haggerty, these did relate to the value and consideration of these swap contracts. The counterparty credit risks that were misrepresented directly related to the value of the contracts, Archegos' ability to perform. This is not just some theoretical relation either. The risks that were concealed materialized, and the counterparties learned, to their detriment, and lost billions of dollars as a result.

Turning to the primary liability claim, your Honor, I think paragraphs 125 and 127 of our complaint describe trade confirmations that Mr. Halligan made and signed. And I don't think there's any dispute that he is the maker of those confirmations. Those confirmations misrepresented that Archegos' total positions — that is, its equity positions plus its swap positions — did not exceed more than 5 percent of the

issuers' outstanding shares. He did that at a time when Archegos' position in certain of these issuers that were subject to the confirms were many multiples in excess of that. And he's certainly the maker of those statements.

On scheme liability: I think Mr. Rankin summarized the issue well. The only thing I would add to it is I think *Rio Tinto* is far narrower than defendants are portraying. *Rio Tinto* describes itself as a very narrow opinion. It considered only the discrete question as to whether *Lorenzo v. SEC*, the Supreme Court's decision from 2019, abrogated the Second Circuit's prior precedent in *Lentell v. Merrill Lynch*. What *Rio Tinto* said was *Lorenzo* clarifies, but does not completely arrogate, its prior precedent.

The clarification that *Lorenzo* adds is that dissemination of a false statement can establish a defendant's primary liability for a scheme. And this, your Honor, is a form of dissemination.

In *Lorenzo*, a subordinate did two things — he copied and pasted a false statement created by his boss into an email, and then he sent that email, at his boss' direction, and that conduct alone was deemed -- based on that conduct alone, that defendant was deemed sufficiently responsible to be held primarily liable for the scheme to defraud the email's recipients. Nothing in *Lorenzo* and nothing in *Rio Tinto* suggests that standard is any different or that its holding

should be limited to subordinates. That is, by any measure, a superior, who creates a misstatement and directs it to be made, is as, if not more, responsible for the fraudulent scheme than the underling who acts at his boss' director. So, by logic, we submit, if a person who sends a false statement on the directive of his boss can be liable, under 10b-5(a) and (c), then so, too, can the boss who orchestrated the scheme and issued the directive.

THE COURT: Thank you.

Mr. Haggerty, did you want to respond briefly?

MR. HAGGERTY: If I may, your Honor.

THE COURT: If it's brief.

MR. HAGGERTY: It is.

Your Honor, on the in-connection with issues, the CFTC argued that the defendants have claimed that *Zandford* has been overruled. The standard that we've advanced is entirely consistent with the outcome of *Zandford*. *Zandford* is a case where the misrepresentation was -- or the alleged deceptive conduct was, in fact, related to the consideration received.

Here, in contrast, the regulators' complaints don't even meet the *Zandford* standard, and as your Court correctly points out, coincide, to the extent that is standard — I'm not sure that it is one — it's really not quite so clear what that means.

But, here, look at the allegations with respect to,

for example, the trade confirmations that Mr. Halligan is alleged to have signed with respect to a particular counterparty. The CFTC relies on that allegation with respect to both the in-connection with argument and with respect to the maker argument. But nowhere in their complaint does the CFTC allege that Archegos ever entered into an ETF swap or a basket swap with that particular counterparty, Swap Counterparty 9.

So, if the requirement is that a misrepresentation must coincide with the securities transaction, or if, under the *Romano* standard, it's that a securities transaction -- a complaint must necessarily allege a securities transaction, then there must be a securities transaction. And, here, there's not even an alleged securities transaction with Swap Counterparty 9.

So, under any standard, that allegation shouldn't be part of the CFTC's case.

Counsel responded to the *Charles Schwab* case and explained the context of that case correctly. That case did involve allegations of understatement of LIBOR rates. And the distinction between -- the different outcomes between the allegations arising from the floating rate instruments and the fixed rate instruments is significant, and that illustrates our point. With respect to the floating rate instruments, the reason that the in-connection with requirement was satisfied was because the misrepresentations related to the consideration

or the value of those instruments; with respect to the fixed rate instruments, they didn't. So we agree, I think, on *Charles Schwab*.

I'll turn, your Honor, to the maker issues very briefly. I think both regulators discussed the *Lorenzo* decision. What is really clear, both from *Janus*, as well as the D.C. Circuit's decision in *Lorenzo* on an issue that wasn't ultimately subject to the litigation before the Supreme Court in that case, is that attribution is key. Attribution of the statement is one of the key characteristics or indicia of the control, the ultimate control, that makes an individual a maker.

And, here, in neither complaint is there any allegation that the statements that Mr. Becker uttered were attributed to Mr. Halligan. So, applying *Janus*, applying *Lorenzo*, those allegations are insufficient.

With respect to *Rio Tinto*: The law is clear that what's required now in the Second Circuit is an inherently deceptive act by the defendant that's separate from the participation in the making of misrepresentations.

And in the *Turquoise Hill* case, Judge Liman identified some examples of conduct that can be inherently deceptive — things like sham contracts or -- your Honor, I want to be accurate — well, your Honor, what I refer the Court to is the decision in *Turquoise Hill*, which refers to the various types

of conduct that is inherently deceptive and could satisfy, after *Rio Tinto*, the scheme liability claim, things like sham invoices or sham contracts, fake transactions, none of which is alleged here. And, in fact, listening to counsel, I was writing fast, and I don't know if I got it all down, but I heard things like scheme to deceive, concealed the conduct related to the misrepresentations, condoned the conduct related to the misrepresentations, conspired to make misrepresentations. And that's all the sorts of participation in the preparation of misstatements that is insufficient after *Rio Tinto*.

Counsel also relied on Mr. Halligan's role as a CFO generically as a basis to infer that he had some role in the conduct sufficient to support a scheme liability claim. We've cited a number of cases that stand very clearly for the proposition that generic reliance on a defendant's role, including generic allegations that a defendant, based on their role, is intimately familiar with various aspects of the business, are simply insufficient. The Court's decision in the *Ollie's Bargain Outlet* case discusses these issues; *Ryanair*, I believe, discusses these issues; *Sotheby's* discusses these issues.

And then, finally, counsel for the CFTC discussed the *Collins & Aikman* case. That case was 15 years before the Second Circuit's decision in *Rio Tinto*, but, more

fundamentally, the allegations there didn't involve solely the making of misrepresentations. So it doesn't stand for the proposition necessary to the disposition of this case, about how the rules of *Janus* and *Rio Tinto* and *Lorenzo* can be synthesized in a way that ensures that scheme liability doesn't become an end run around *Rio Tinto*. And that's why now, in this circuit, participation in the preparation of misrepresentations alone isn't sufficient to make out a scheme link.

THE COURT: Thank you.

MR. HAGGERTY: Thank you.

THE COURT: We don't have that much more time, but I did want to give the SEC and CFTC an opportunity to address the issues on which you all have a dispute, if you want to add anything. It's briefed with the amicus brief and the response, but if there's anything you all would like to add, you can.

Starting with the SEC, I guess.

MR. ZETLIN-JONES: I would defer to my colleague from our general counsel's office on this.

THE COURT: You can also just rest on the amicus brief, that's fine.

MR. LISITZA: I rest. If there was a particular issue or concern that you wanted the SEC to --

THE COURT: No, I think it's briefed, and I don't have any particular questions about it at this point.

MR. LISITZA: Okay.

THE COURT: Okay.

Do you want to add anything on it?

MR. MURPHY: Just briefly, your Honor.

The only issue before this Court is the CFTC's jurisdiction. The SEC is not a party to our case. And so the Court has no need to rule on whether the SEC has jurisdiction over the ETF swap products.

Defendants and also the SEC are effectively asking this Court to strip the CFTC of its ability to prosecute fraud in these swaps markets, and the Court should reject that.

The CFTC has a long history of regulating derivatives on broad-based securities indexes, and we have a substantial expertise in that area, as well as substantial expertise in regulating and policing the swaps markets.

The defendants' arguments, if accepted, would prevent the CFTC from carrying out its statutory authority of protecting the derivatives markets, and we would be unable to pursue wrongdoing, such as the wrongdoing at issue in this case.

I would note that we were the only regulatory agency to bring claims in relation to the ETF swaps, and if we were stripped of jurisdiction over those products, the markets would be less protected and worse off.

With that, your Honor, I'm happy to answer any

questions about the ETF swaps or custom basket swaps that you may have.

THE COURT: Thank you.

I gather your position is that I don't need to decide this issue because, even on the SEC's views, some subset of the custom basket swaps would be at issue, so I don't necessarily need to decide this issue if the case were going to go forward.

Is that right?

MR. MURPHY: That's part of it, your Honor. There are two types of broad-based swaps at issue — there are the ETF swaps and the custom basket swaps. So you're correct that even if the CFTC were found to lack jurisdiction over the ETF swaps, we would still have authority over the custom basket swaps, and the case should go forward.

But, in addition, I would note that our main point is the CFTC has jurisdiction regardless of whether the SEC has jurisdiction. There is a category of swaps called mixed swaps, in which both the SEC and CFTC have jurisdiction. So, really, there is no need to determine the issue of the SEC's jurisdiction at all. The only question is, does the CFTC have jurisdiction over the ETF swaps?

THE COURT: Let me just ask if either Archegos or Mr. Halligan want to address these issues?

MR. JOHNSON: Yes, your Honor. Thank you. William Johnson, on behalf of Archegos.

I'll try to be brief.

The ETFs are security-based swaps. The ETFs are funds; they issue securities. The funds themselves are registered with the SEC as issuers of securities, and the shares of those funds are also registered as securities. That makes these instruments security-based swaps.

THE COURT: You agree with the SEC?

MR. JOHNSON: A hundred percent.

They are not based on the value of the index. They are based on the value of the shares. They are traded in the secondary market, and you get whatever price you get in the secondary market for them.

The CFTC uses the term wrapper as if it's just a label. These are not labels. The shares are what matter here. The shares are what determine that these are security-based swaps. There's no economic reality or other independent test in the joint rules release or in Dodd-Frank. The value of these are expressed as the value of the shares, end of story. They're not mixed swaps because they don't involve anything other than the security, the share, that's the value that drives the value. There's no other instrument that's at play. It is simply another version of the index argument, which has failed.

With respect to the custom baskets, your Honor: The law is clear that where one or both parties has the ability to

affect the composition of the basket, it effectively turns these into single-name swaps, a big list of single-name swaps. If you can move them in and out with your authority or the combination of the other counterparty, they're effectively single-name swaps, and they're based on shares, and they're, therefore, security-based swaps.

As the SEC points out, this is a binary concept. They're either discretionary or they are determined -- the composition is determined by a predetermined or automatic criteria.

And whenever there is a determination that can be done based on discretion, based on the joint rules release, that makes them a narrow-based and a security-based swap.

THE COURT: Okay. Thank you.

I don't think I have any additional questions on those issues. Before we break, did anyone else have a burning need to say anything else?

MR. MURPHY: Your Honor, may I briefly respond on the ETF and custom basket swaps?

THE COURT: Yes.

MR. MURPHY: So, we have alleged that the ETF swaps are based on broad-based indexes, and, really, that's the issue here, it's are our allegations sufficient? And we have alleged that these are based on broad-based security indexes.

If you look at the documents that defendants have

cited, those documents actually show that our allegations are not just plausible and sufficient, they show that our allegations are actually correct. They show that the ETF swaps are based on three different types of broad-based indexes. The first is the underlying market index — the S&P 500, for example; the second is the portfolio of securities held by those ETFs — those are groups of securities, and they're broad based, so they fall within our jurisdiction; and then the third is the ETF shares themselves. So an index includes not just a group of securities, but also an interest in a group of securities.

In the prospectuses that defendants have attached, they each explicitly state that the ETF shares are, quote, an interest in an underlying security portfolio, in other words, they meet the definition of a broad-based index. And you can find the quotes in our briefs, your Honor, so I won't read them here.

With respect to the custom basket swaps: Again, the issue is what we have alleged. We have alleged that these custom basket swaps are broad-based security index swaps, and that's sufficient at this stage. But, again, if your Honor is inclined to consider these swap agreements that defendants have attached, they still show that our allegations are not just plausible, our allegations are correct.

None of those agreements use anything like the phrase

discretion to change the portfolio or at-will modification or anything like that. The most that these agreements provide for is that the counterparties needed to agree to some sort of modification, but an agreement is not discretion, an agreement is not an unfettered ability, which is what discretion really means.

So if you look at the terms of those agreements, it shows that no party actually had discretion.

THE COURT: All right. Thank you.

Anything else?

MR. LISITZA: Just to be sure, did you want the SEC to address anything about either the binary nature of the swaps and custom baskets or the mixed swap?

THE COURT: Not at this point.

All right. Decision is reserved. Thank you, all. The briefing and argument were very well done. And I'll reserve decision.

Did the U.S. Attorney's Office want to speak today?

MR. THOMAS: No, your Honor.

THE COURT: Thank you, everyone. We're adjourned.

(Adjourned)